sary prices to be discovered. How, in a regime of constant change, these equations were to operate, the proponents of this approach left unsaid. The most popular response to Mises, though, lay elsewhere. The Polish economist Oskar Lange, long resident in the United States until, following the Second World War, the blandishments of Communist Poland proved too much for him to resist, claimed that a socialist economy need not abandon the market. Though to some "market socialism" has little more sense the a "square circle," Lange was of course not among them. But his proposal, though original, fared no better than the others. Mises subjected it to withering attack, the details of which I leave the interested reader to explore in Mises's work. In particular, his illuminating discussion of his critics in *Human Action* should be consulted.

Mises exposed several irremediable and crucial errors in Marxism. A reader of his criticism cannot help but apply to Marxism the well-known line from "Ozymandias": "Round the decay of that colossal wreck, . . . /The lone and level sands stretch far away."

Keynesian Myths

Murray N. Rothbard

Inflation and Idle Capacity

The Keynesians have been caught short again. In the early and the late 1970s, the wind was taken out of their sails by the arrival of inflationary recession, a phenomenon which they not only failed to predict, but whose very existence violates the fundamental tenets of the Keynesian system. Since then, the Keynesians have lost their old invincible arro-

gance, though they still constitute a large part of the economics profession.

In the last few years, the Keynesians have been assuring us with more than a touch of their old *hauteur*, that inflation would not and could not arrive soon, despite the fact that "tight-money" hero Paul Volcker had been consistently pouring in money at double-digit rates. Chiding hard-money advocates, the Keynesians declared that, despite the monetary inflation, American industry still suffered from "excess" or "idle" capacity, functioning at an overall rate of something like 80%. Thus, they pointed out, expanded monetary demand could not result in inflation.

As we all know, despite Keynesian assurances that inflation could not reignite, it *did* despite the idle capacity, leaving them with something else to puzzle over. Inflation has risen this year from approximately 1% in 1986 to 6% now, interest rates are rising again, the fall of the dollar has raised import prices, and gold prices are rising again. Once again, the hard-money economists and investment advisors have proved far sounder than the Establishment-blessed Keynesians.

The best way to explain where the Keynesians went wrong is to turn against them their own common reply to their critics: that anti-Keynesians, who worry about the waste of inflation or government programs, are "assuming full employment" of resources. Eliminate this assumption, they say, and Keynesianism becomes correct in the through-the-looking-glass world of unemployment and idle resources. But the charge should be turned around, and the Keynesians should be asked: why should there be unemployment (of labor or of machinery), at all? Unemployment is not a given that descends from heaven. Of course, it often exists, but what can account for it?

The Keynesians themselves create the problem by leaving out the price system. The hallmark of crackpot economics is an analysis that somehow leaves out prices, and talks only about such aggregates as income, spending, and employment.

We know from "microeconomic" analysis that if there is a "surplus" of something on the market, if something cannot be sold, then the only reason is that its price is somehow being kept too high. The way to cure surplus or unemployment of anything, is to lower the asking price, whether it be wage rates for labor, prices of machinery or plant, or of the inventory of a retailer

In short, as Professor William H. Hutt pointed out brilliantly in the 1930s, when his message was lost amid the fervor of the Keynesian Revolution: idleness or unemployment of a resource can only occur because the owner of that resource is deliberately withholding it from the market and refusing to sell it at the offered price. In a profound sense, therefore, all unemployment and idleness is voluntary.

Why should a resource owner deliberately withhold it from the market? Usually, because he is holding out for a higher price, or wage rate. In a free and unhampered market economy, the owners will find out their error soon enough, and when they get tired of making no returns from their labor or machinery or products, they will lower their asking price sufficiently to sell them. In the case of machinery and other capital goods, of course, the owners might have made a severe malinvestment, often due to artificial booms created by bank credit and central banks. In that case, the lower market-clearing price for the machinery or plant might be so low as to not be worth the laborer's giving up his leisure—but then the unemployment is purely voluntary and the worker holds out permanently for a higher wage.

A worse problem is that, since the 1930s, government and its privileged unions have intervened massively in the labor market to keep wage rates above the market-clearing wage, thereby insuring ever higher unemployment among workers with the lowest skills and productivity. Government interference, in the form of minimum wage laws and compulsory unionism, creates compulsory unemployment, while welfare

payments and unemployment "insurance" subsidize unemployment and make sure that it will be permanently high. We can have as much unemployment as we pay for.

It follows from this analysis that monetary inflation and greater spending will not necessarily reduce unemployment or idle capacity. It will *only* do so if workers or machine owners are induced to think that they are getting a higher return and at least some of their holdout demands are being met. And this can only be accomplished if the price paid for the resource (the wage rate or the price of machinery) *goes up*. In other words, greater supply or use of capacity will only be called forth by wage and price increases, i.e. by *price inflation*.

As usual, the Keynesians have the entire causal process bollixed up. And so, as the facts now poignantly demonstrate, we can and do have inflation along with idle resources.

The New International Money Scheme

Ever since the Western world abandoned the gold coin standard in 1914, the international monetary system has been rocketing from one bad system to another, from the frying pan to the fire and back again, fleeing the problems of one alternative only to find itself deeply unhappy in the other. Basically, only two alternative systems have been considered: (1) fiat money standards, each national fiat currency being governed by its own central bank, with relative values fluctuating in accordance with supply and demand; and (2) some sort of fixed exchange rate system, governed by international coordination of economic policies.

Our current System 1 came about willy nilly in 1973, out of the collapse of Bretton Woods System 2 that had been imposed on the world by the United States and Britain in 1944. System 1, the monetarist or Friedmanite ideal, at best breaks up the world monetary system into national fiat enclaves, adds great uncertainties and distortions to the monetary sys-

tem, and removes the check of external discipline from the inflationary propensities of every central bank. At worst, System 1 offers irresistible temptations to every government to intervene heavily in exchange rates, precipitating the world into currency blocs, protectionist blocs, and "beggar-thy-neighbor" policies of competing currency devaluations such as the economic warfare of the 1930s that helped generate World War II.

The problem is that shifting to System 2 is truly a leap from the frying pan into the fire. The national fiat blocs of the 1930s emerged out of the System 2 pound sterling standard in which other countries pyramided an inflation of their currencies on top of inflating pounds sterling, while Britain retained a nominal but phony gold standard. The 1930s system was itself replaced by Bretton Woods, a world dollar standard, in which other countries were able to inflate their own currencies on top of inflating dollars, while the United States maintained a nominal but phony gold standard at $35 per gold ounce.

Now the problems of the Friedmanite System 1 are inducing plans for some sort of return to a fixed exchange rate system. Unfortunately, System 2 is even worse than System 1, for any successful coordination permits a concerted world-wide inflation, a far worse problem than particular national inflations. Exchange rates among fiat moneys have to fluctuate, since fixed exchange rates inevitably create Gresham's Law situations, in which undervalued currencies disappear from circulation. In the Bretton Woods system, American inflation permitted world-wide inflation, until gold became so undervalued at $35 an ounce that demands to redeem dollars in gold became irresistible, and the system collapsed.

If System 1 is the Friedmanite ideal, then the Keynesian gold is the most pernicious variant of System 2. For what Keynesians have long sought, notably in the Bernstein and Triffin Plans of old, and in the abortive attempt to make

SDRs (special drawing rights) a new currency unit, is a World Reserve Bank issuing a new world paper-money unit, replacing gold altogether. Keynes called his suggested new unit the "bancor," and Harry Dexter White of the U.S. Treasury called his the "unita." Whatever the new unit may be called, such system would be an unmitigated disaster, for it would allow the bankers and politicians running the World Reserve Bank to issue paper "bancors" without limit, thereby engineering a coordinated world-wide inflation. No longer would countries have to lose gold to each other, and they could fix their exchange rates without worrying about Gresham's Law. The upshot would be an eventual world-wide runaway inflation, with horrendous consequences for the entire world.

Fortunately, a lack of market confidence, and inability to coordinate dozens of governments, have so far spared us this Keynesian ideal. But now, a cloud no bigger than a man's hand, an ominous trial balloon toward a World Reserve Bank has just been floated. In a meeting in Hamburg, West Germany, in late June of two hundred leading world bankers in an International Monetary Conference, bankers urged the elimination of the current volatile exchange rate system, and a move towards fixed exchange rates.

The theme of the Conference was set by its chairman, Willard C. Butcher, chairman and chief executive of Rockefeller's Chase Manhattan Bank. Butcher attacked the current system, and warned that it could not correct itself, and that a search for a better world currency system "must be intensified" (*New York Times*, June 23, 1987).

It was not long before Toyo Gyoten, Japan's vice-minister of finance for international affairs, spelled out some of the concrete implications of this accelerated search. Gyoten proposed a huge multinational financial institution, possessing "at least several hundred billion dollars," that would be empowered to intervene in world financial markets to reduce volatility.

And what is this if not the beginnings of a World Reserve Bank? Are Keynesian dreams at least beginning to come true?

Liberty and Property

Ludwig von Mises

The pre-capitalistic system of production was [based on] military conquest. The victorious kings had given the land to their paladins. These aristocrats were lords in the literal sense of the word, as they did not depend on the patronage of consumers buying or abstaining from buying on the market. On the other hand, they themselves were the main customers of the processing industries which under the guild system were organized on a cooperative basis.

This scheme was opposed to innovation. It forbade deviation from the traditional methods of production. The number of people for whom there were jobs even in agriculture or in the arts and crafts was strictly limited. Under these conditions, many a man, to use the words of Malthus, had to discover that at "nature's mighty feast there is no vacant cover for him," and that "she tells him to be gone." But some of these outcasts nevertheless managed to survive, begot children, and made the number of the destitute grow hopelessly more and more.

But then came capitalism.

It is customary to see the radical innovations that capitalism brought about as substitution of the mechanical factory for the more primitive and less efficient methods of artists and shops. This is a rather superficial view. The characteristic feature of capitalism, that distinguishes it from pre-capitalistic methods of production, was its new principle of marketing.